AG Insurance NV

Full Rating Report

Ratings

AG Insurance

Insurer Financial Strength Rating	A+
Long-Term Issuer Default Rating	A
Subordinated bonds	BBB+

Sovereign Risk

Long-Term IDR	AA

Outlooks

Insurer Financial Strength Rating	Stable
Long-Term IDR	Stable
Sovereign Long-Term IDR	Stable

Financial Data

AG Insurance (Consolidated)

(EURm)	31 Dec 17	31 Dec 16
Total assets	75,625	76,607
Total equity	7,060	6,501
Pre-tax profit	796	716
Net premiums earned	4.933	5,608
Solvency II margin (%)	229	207

Source: AG Insurance

Related Research

Belgium Insurance Dashboard - FYE2017 (March 2018)
Fitch Affirms Belgium at 'AA-'; Outlook Stable (June 2018)

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Key Rating Drivers

Core to Ageas Group: Fitch Ratings regards AG Insurance as the main insurance operating entity of the Ageas group and 'Core' to the group. Its ratings are therefore derived from a combined assessment of the consolidated Ageas group.

Very Strong Capital Adequacy: The ratings of AG Insurance benefit from its very strong solvency. Its regulatory Solvency II (S2) margin, calculated according to its partial internal model on non-life underwriting risk, was 229% at end-2017. AG Insurance's financial leverage ratio was 22% at end-2017 (22% in 2016). We expect financial leverage to remain stable in the medium term.

Adequate Financial Flexibility: Fitch views AG Insurance's financial flexibility as adequate. AG Insurance accessed debt capital markets through subordinated bond issues in 2015 and in 2013. The company was not involved in litigation risk affecting its ultimate parent ageas SA/NV (IDR A/Stable), which is positive from the perspective of financial flexibility.

Strong but Under-Pressure Profitability: Profitability in 2017 continued to be strong and resilient to the low-yield environment. Underwriting conditions in Belgium remain challenging, however, and investment income is under pressure because of low interest rates. Fitch believes these conditions are likely to continue to weigh on profitability.

Mitigated Interest-Rate Risk: AG Insurance's life technical liabilities are subject to minimum guaranteed returns. However, AG Insurance maintains a policy where duration gap should not exceed one year. Individual investment products have a market-value adjustment clause if redeemed before eight years, meaning the surrender value would be equal to the value of the assets at the time of redemption. This protects the insurer against lapses due to unfavourable market movements.

Strong Position in Belgium: AG Insurance is the largest insurer in Belgium. Access to extensive and diversified distribution channels, including the banking network of BNP Paribas Fortis SA/NV (Long-Term IDR: A+/Stable), benefits AG Insurance's rating.

This agreement has no explicit end date, but carries a three-year termination notice period. The put option held by BNP Paribas Fortis to sell the 25% plus one share of AGI to Ageas expired at end-June 2018. In the event the notice is given, Fitch expects Ageas's franchise to remain strong in Belgium, as the group would leverage off its existing customers and exploit alternative distribution channels, such as brokers.

Rating Sensitivities

Improved Profitability: The ratings could be upgraded if Ageas' profitability improves over a sustained period, with a return on equity above 10%, a pre-tax operating return on assets of 1.1% (2017: 1.0%) or above.

Deterioration in Capital Adequacy: Ageas's ratings could be downgraded if Ageas's Prism FBM score falls to the 'Strong' category on a sustained basis.

Reduction in Profitability: Ageas's ratings could also be downgraded if its profitability weakens significantly on a sustained basis, with return on equity below 5% and pre-tax operating return on assets below 0.4.

Business Profile

Very Strong Business Profile in Belgium

Belgium accounted for 75% of the total cash remitted to the group in 2017. It also represents around 75% of technical liabilities.

Belgium-based AG Insurance (Ageas's main operating entity) has a strong franchise in the country and can exploit its pricing power. It is Belgium's largest life insurer, with a market share measured by gross written premiums of around 30% in 2016. AG Insurance is also the second-largest non-life insurer in the country, with 16.5% of the market, behind AXA Belgium (IFS Rating: AA−/Stable) with 18.7%, but ahead of Ethias SA (IFS Rating: BBB+/Stable) with 12.6% and KBC Insurance NV with 9.1%.

AG Insurance's life insurance total gross inflows (insurance plus investment contracts) were EUR3.8 billion in 2017 (2016: EUR4.2 billion). In 2017, inflows fell following lower sales of guaranteed products compared with 2016.

Non-life gross earned premiums stood at EUR1.9 billion in 2017, slightly better than 2016. AG Insurance is more active in accident and health insurance than its peers, which benefits portfolio diversification, although it can make results more volatile.

In 2017, AG Insurance generated 49% of life inflows and 16% of non-life inflows through the bank channel, of which a substantial part arose through an exclusive distribution agreement in Belgium with BNP Paribas Fortis SA/NV (LT IDR: A+/Stable). This agreement has no explicit end date, but carries a three-year termination notice period. The put option hold by BNP Paribas Fortis to sell the 25% plus one share of AGI to Ageas expired at end-June 2018. In the event the notice is given, Fitch expects AG Insurance franchise to remain strong, as the company would leverage off its existing customers and exploit alternative distribution channels, such as brokers.

Related Criteria

Insurance Rating Criteria
(November 2017)

Ownership is Ratings Neutral

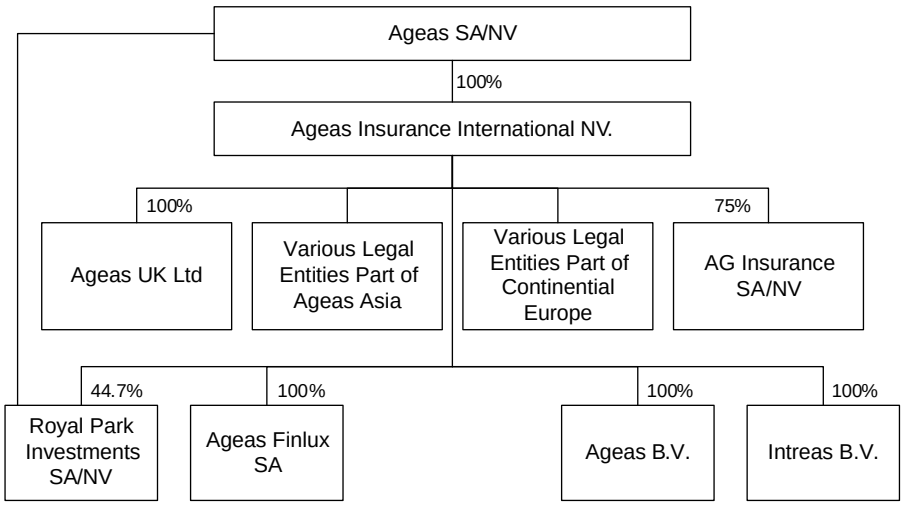
Corporate Governance and Management

Corporate governance and management are adequate and are neutral to the rating.

ageas SA/NV is quoted in the Brussels Stock Exchange with a market capitalisation of EUR8.7 billion at end June-2018. ageas SA/NV is the ultimate holding company of Ageas group, while Ageas Insurance International N.V. is the group intermediate holding company, through which the insurance operations are owned. Ageas is now active only in insurance and holds a 75% stake in AG Insurance, and has interests in insurance companies in the UK, continental Europe and Asia.

BNP Paribas Fortis has owned 25% of AG Insurance since May 2009, while the other 75% is owned by Ageas (formerly the Fortis group). BNP Paribas Fortis is 100% owned by BNP Paribas. The put option granted by Ageas to BNP Paribas Fortis to sell the 25% plus one share of AG Insurance to Ageas expired at end June-2018, without being exercised. In accordance with IFRS, Ageas will derecognise from its balance sheet the liability written for the put option and will increase the value of the non-controlling interest in its shareholders' equity.

Ageas' Group Structure



Source: Ageas

Sovereign and Country-Related Constraints

Fitch rates the local-currency sovereign obligations of Belgium at 'AA-' with a Stable Outlook, and the Country Ceiling is 'AAA'.

Given these very high ratings, the ratings of insurance organisations and other corporate issuers in Belgium are not likely to be constrained by sovereign or macroeconomic risks, and in the specific case of AG Insurance no constraints apply.

Industry Profile and Operating Environment

Belgium: Life Market Contracting; Non-Life Stable

The Belgian life insurance market is facing challenges from falling premiums as a result of the reduction in minimum guarantees, competition from bank savings products, and unfavourable tax treatment. Total premiums have decreased since 2012, and although we expect the life market to have stabilised in 2017 after stronger demand for guaranteed products this decline is likely to continue in 2018, despite the increasing appetite of life insurers for selling unit-linked products. We expect the non-life market to continue growing slowly.

Belgian life insurers face a difficult operating environment, as persistently low interest rates constrain profitability and demand for life products. This trend is negative for margins on guaranteed products. Operating results in 2017 were resilient, but we believe this followed a higher realisation of investment gains. We believe that recent decreases in the average guaranteed rate for new contracts (now 0.25%) will continue to suppress the demand for guaranteed products in 2018, but this should partly be offset by growth in unit-linked products.

The non-life market in Belgium is competitive but disciplined. Tariffs are under pressure but they remain technically robust. The market can be prone to natural catastrophe claims (eg storms and floods in 2016). Results for 2016 were also affected by the terrorist attacks on Brussels. Fitch estimates the combined ratio in 2017 to have improved to an average of around 92% from 96% (2016) for the market as the claims experience was more benign than in 2016. We expect a combined ratio of between 90% and 95% in 2018, assuming a normalised level of weather-related claims.

Peer Analysis

Larger Scale, Strong Capital

AG Insurance's peers are the mid- to large Benelux composite insurers. AG Insurance is larger than its peers in the sample. Those insurers have limited exposure to non-domestic markets.

In 2017, profitability, as measured by return on equity, was stronger than the peer average. This was also due to AG Insurance's improved combined ratio to 91% (2016: 96%). Capitalisation, as measured by the Solvency II ratio, was strong and higher than peers.

Peer Comparison

End-2017 (EURm)	IFS Rating[a]	Assets	Total equity[b]	Net income	Return on assets[c] (%)	Combined ratio (%)	Return on equity[d] (%)	Financial leverage (%)	Solvency II ratio (%)
AG Insurance	**A+/Stable**	**75,625**	**7,060**	**583**	**1.2**	**91**	**9**	**22**	**229**
Ethias S.A.	BBB+/Positive	18,755	2,521	158	1.4	88	7	20	205
SRLEV NV (VIVAT)	BBB+/Evolving	56,747	3,547	-116	n.m.	99	-3	21	162

[a] IFS Rating of main operating companies of each group
[b] Includes minorities
[c] Group net income/2016-2017 average total assets
[d] Group net income/2016-2017 average group shareholders' equity
Source: Companies, Fitch

Capitalisation and Leverage

(EURm)	2013	2014	2015	2016	2017	Fitch's expectation
Total assets	67,237	74,024	73,783	76,331	75,625	Debt leverage, as calculated by Fitch, is expected to remain at 20%-25% in the medium term. Solvency position should remain very strong.
Total equity	5,025	6,488	6,810	6,501	7,060	
Financial leverage ratio (%)	25	22	24	22	22	
Regulatory solvency ratio (x)[a]	1.9	2.1	2.4	2.1	2.3	
Total Financing and Commitments (TFC) ratio (x)	1.0	0.9	1.0	1.0	0.8	

[a] Solvency I until 2014; Solvency II since 2015
Source: Fitch, AG Insurance

Very Strong Capital Adequacy, Low Leverage

- Very strong capital
- Low debt leverage
- High TFC ratio, but improving

Very Strong Capital

Fitch considers AG Insurance's capital adequacy to be strong, based on the regulatory solvency ratio. At end-2017, its regulatory S2 margin, calculated according to its partial internal model on non-life underwriting risk, was 229%, up from 207% at end-2016. AG Insurance does not make use of transitional measures to calculate its regulatory solvency position.

AG Insurance's risks are well diversified due to its involvement in life and non-life businesses. However, geographical diversification is negligible, due to the company's focus on the Belgian market.

Low Debt Leverage

AG Insurance's financial leverage ratio was relatively low at 22% at end-2017 (2016: 22%) according to Fitch's calculation. The ratio does not include leverage related to real-estate operations, which we consider as operational. Fitch expects financial leverage to remain stable in the medium term.

High TFC, but Improving

The total financing and commitments (TFC) ratio, which is designed to measure the total debt, financing, and capital markets footprint of an organisation and its overall reliance on access to funding sources, was relatively high at 0.8x at end-2017 (2016: 1.0x). This reflects AG Insurance's use of repurchase agreements to hedge specific investments with resettable interest rates and for cash management, and the use of operational debt. The improvement compared to 2016 was mainly driven by the higher shareholders' equity.

Fitch views AG Insurance repurchase agreements as reasonably matched from an asset and liability management (ALM) perspective as funds are invested in highly rated securities.

Debt Service Capabilities and Financial Flexibility

(x)	2013	2014	2015	2016	2017	Fitch's expectation
Fixed-charge coverage ratio (including realised and unrealised gains)	9	8	8	9	10	Fitch expects AG Insurance's run-rate fixed-charge coverage ratio to remain above 7x.

Source: Fitch

Adequate Financial Flexibility

- Subordinated debt issued directly
- Strong fixed-charge coverage

Subordinated Debt Issued Directly

AG Insurance issued subordinated debt directly in its own right in 2013 and 2015, demonstrating its good access to debt capital markets. Before these issues, the debt issued by AG Insurance was fully owned by Ageas Hybrid Financing and therefore the company had no external outstanding debt.

Strong Fixed-Charge Coverage

AG Insurance's fixed-charge coverage (FCC) ratio, including realised and unrealised gains and losses, was 10x in 2017 (2016: 9x). We expect the FCC ratio to remain above 7x, a level that Fitch views as strong and commensurate with the ratings.

Financial Performance and Earnings

(EURm)	2013	2014	2015	2016	2017	Fitch's expectation
Net income	447	522	512	521	583	Fitch expects AG Insurance's profitability to remain strong but under pressure as interest rates remain low. We expect the combined ratio to be below 95% in 2018.
Combined ratio (non-life) – reported (%)	101	103	95	96	91	
Net income return on equity (%)	9	9	8	8	9	
Pre-tax operating return on assets (including realised and unrealised gains) (%)	1.1	1.1	1.1	1.1	1.2	

Source: Fitch, Ageas

Strong but Pressured Profitability

- Strong net profitability
- Solid life profitability
- Strong underwriting profitability for non-life business

Strong Net Profitability

Fitch considers that AG Insurance's profitability is strong and stable over time. This is despite investment income being under pressure due to low interest rates. Fitch believes these investment conditions are likely to continue over the course of 2018 and in 2019.

Profitability, measured by net income ROE, remained strong at 9% in 2017 (2016: 8%). Nonetheless, AG Insurance's earnings are sensitive to financial-market volatility, as investment earnings come largely from realised investment gains, which may not recur. Fitch's analysis of earnings growth suggests that AG Insurance has expanded its life and non-life businesses in line with the Belgian market over the past five years.

Solid Life Profitability

The life operating margin on guaranteed products, measured by Fitch-calculated operating return on assets (ROA), was a strong 1.2% in 2017 (2016: 1.1%), supported by realised gains. AG Insurance has a loyal customer base in Belgium; its savings contracts have an average maturity of more than eight years and lapse rates are low.

Strong Underwriting Profitability for Non-Life Business

AG Insurance's non-life underwriting profitability is strong. The combined ratio improved to 91% in 2017, better than Fitch's expectations, from 96% in 2016. The ratio benefited from benign claims experience, while 2016 was negatively affected by the terrorist attacks and weather-related events. AG Insurance is exposed to retained risk on natural catastrophes, which creates some volatility in the ratio. We expect the combined ratio to remain below 95% in 2018.

Competition remains strong in most lines of business in Belgium, preventing underwriting profitability from improving greatly. AG Insurance's strong market position in workers' compensation and other liabilities lines in Belgium partly explains its relatively high combined ratios in these lines (95% and 103%, respectively, in 2017, improving year-on-year) as they are long-tail.

Investment and Asset Risk

(%)	2013	2014	2015	2016	2017	Fitch's expectation
Unaffiliated shares/equity	49	45	43	46	52	Fitch expects AG Insurance's exposure to risky assets to remain commensurate with the current rating level.
Non-investment-grade bonds/equity	22	14	18	19	19	
Investments in affiliates/equity	6	5	6	7	8	
Risky assets[a]/equity	78	64	68	72	78	

[a] This ratio is a combination of the speculative-grade bonds (including unrated commercial loans), unaffiliated common stock, and investment in affiliates
Source: Fitch

Prudent Investment Policy Overall

- Cautious investment allocation
- Strong risky assets-to-equity ratio
- Significant real-estate and loans exposure

Cautious Investment Allocation

AG Insurance's consolidated investments, excluding unit-linked investments, stood at EUR64 billion at end-2017. The investment breakdown was 74% fixed-income securities, 13% loans and mortgages, 7% equity, 4% real estate, and 2% cash.

Bonds are the major asset class on AG Insurance's balance sheet, 65% of which are government bonds. The credit quality of the bond portfolio is good, with 79% rated 'A' or higher at end-2017 and 1% sub-investment grade or unrated. AG Insurance's government bond portfolio is highly concentrated, with 59% in Belgium and 17% in France.

Loans are predominantly to government and official institutions of high credit quality; 26% of the loans to banks and commercial loans are sub-investment grade or unrated, but they represent about 30% of the total loans.

Strong Risky Assets-to-Equity Ratio

AG Insurance's risky assets-to-equity ratio, as calculated by Fitch, is strong. This reflects the group's investment focus on Belgian government and corporate debt. It slightly deteriorated to 78% at end-2017 (2016: 72%), however, as AG Insurance increased its exposure to equities.

Significant Real Estate and Loans Exposure

AG Insurance has significant exposure to real estate, in the form of investment properties and mortgage loans (residential and commercial). The market value of AG Insurance's real-estate investment portfolio was EUR3.7 billion at end-2017, which was around 5% of total invested assets, but around 50% of shareholders' funds. Property investment comprises warehouses, office buildings, shopping centres, care homes and car parks. Offices are mainly located in the Brussels area, which is stable in value, thanks to the presence of the EU administration. AG Insurance has diversified its real-estate portfolio with investments in France, Spain and Germany.

The real estate investment portfolio carried gross unrealised capital gains of EUR0.8 billion at end-2017, in line with 2016. Fitch regards AG Insurance's real-estate portfolio as being of good quality and ratings neutral.

Among unrated loans, mortgages were EUR1.2 billion, mainly retail positions in Belgium. They represent 17% of shareholders' funds, although they are protected by more than EUR1.1 billion of overcollateralisation.

Asset/Liability and Liquidity Management

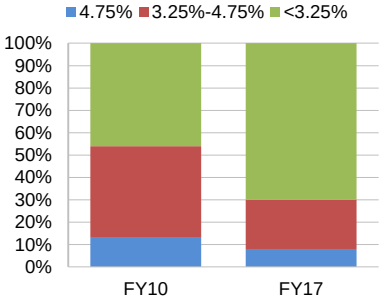
(%)	2013	2014	2015	2016	2017	Fitch's expectation
Liquid assets/policyholder liabilities (total)	99	102	100	97	96	Fitch expects AG Insurance's asset-liability management structure and performance to remain adequate.

Note: Liquid assets exclude loans
Source: Fitch

Adequate Liquidity Profile

- Minimum guaranteed rate reviewed
- Interest-rate risk mitigated

Breakdown of Technical Reserves by Guarantee



Source: AG Insurance

Minimum Guaranteed Rate Reviewed

Life technical liabilities are subject to minimum guaranteed returns. Technical provisions relating to policies carrying guaranteed interest rates are falling in the existing portfolio. The Belgian regulator does not impose formal requirements for guarantees on new individual life products. AG Insurance decreased the interest guarantee offered on new individual retail products written, along with the decrease of the Belgium Obligations Linéaires Ordinaires since January 2012, due to the intense competition.

However, as of 1 March 2018 the company increased minimum guaranteed returns on new retail life investment products (mainly single premium) to 0.5% from 0.25%. In group life contracts, minimum guaranteed returns remained at 0.75% on products with an interest guarantee on reserves and at 0.25% on products with an interest guarantee on reserves and future premiums. There is also no longevity risk in AG Insurance's books as customers receive a lump sum at retirement age that is not annuitised.

Interest-Rate Risk Mitigated

AG Insurance maintains a policy where duration gap should not exceed one year. This enables the company to achieve a better and more stable solvency ratio, at the expense of potential profits (or losses) from taking a position on interest rate movements.

An additional mitigating factor is that individual investment products have a market-value adjustment clause if redeemed before eight years, meaning the surrender value would be equal to the value of the assets at the time of redemption. This feature protects the insurer against lapses if there are unfavourable investment-market movements.

Reserve Adequacy

(%)	2013	2014	2015	2016	2017	Fitch's expectation
Loss reserves/current-year incurred losses	2.6	2.7	3.1	3.1	3.5	Fitch expects AG Insurance's reserve ratio to remain stable and prior-year reserve releases to remain positive overall (with some further potential negative variances in certain liability lines).
Loss reserves/equity	0.6	0.5	0.5	0.5	0.5	
Current-year paid losses/incurred losses	0.9	0.9	0.9	0.9	0.9	
Change in loss reserves/earned premium ratio	0.9	4.9	1.3	3.0	0.3	
One-year reserve development/prior-year loss reserves	4.0	6.2	-2.3	-1.9	-2.3	
One year reserve development/prior-year equity	2.2	3.9	-1.2	-0.9	-1.2	
Net technical reserves/net earned premium (non-life)	193	197	200	203	204	

Note: Negative numbers denote positive reserve developments
Source: Fitch

Adequate Non-Life Reserves

- Adequate reserve growth and experience
- Tail risk in Belgium from workers' compensation

Adequate Reserve Growth and Experience

Fitch believes AG Insurance's loss reserves have grown at a rate commensurate with growth in underwriting exposures over the past five years. Analysis of the group's claims development triangles indicates negative reserve development until 2014, in particular for certain liability lines, however development has been positive since.

Fitch nonetheless believes the level of technical provisions is prudent, in light of regulatory requirements and practices in Belgium, taking into account the company's technical commitments, the return on its investment portfolios, and its expenses.

Tail Risk in Belgium from Workers' Compensation

AG Insurance underwrites workers' compensation lines. These lines have a long tail and are difficult to estimate reserves for. This largely explains some reserve deficiency in certain years.

Despite this deficiency, Fitch views AG Insurance's overall reserving adequacy as robust and supportive of the current rating level.

Reinsurance, Risk Management and Catastrophe Risk

- High retention rate
- Mostly non-proportional cover

High Retention Rate

AG Insurance, in line with the Ageas group, is not a big purchaser of reinsurance, as shown by its high retention rate, which was 97% in non-life insurance in 2017, in line with 2016. This reflects the low risk profile of its book of business, which mostly comprises savings-type life and protection business. Most of the ceded premiums relate to non-life product lines.

Mostly Non-Proportional Cover

AG Insurance purchases reinsurance coverage with excess-of-loss and stop-loss programmes.

The major uses of external reinsurance include the mitigation of the effect of natural disasters (eg hurricanes, earthquakes and floods), large, single claims from policies with high limits and multiple claims triggered by a single man-made event.

The largest reinsurers are Swiss Reinsurance Company Ltd (IFS Rating: AA-/Stable), Munich Reinsurance Company (IFS Rating AA/Stable) and SCOR SE (AA-/Stable).

Appendix A: Other Ratings Considerations

Below is a summary of additional ratings considerations of a "technical" nature that are part of Fitch's ratings criteria.

Group IFS Rating Approach

Fitch considers AG Insurance as strategically key and an integral part of Ageas' business and therefore 'Core' to the consolidated group. Fitch therefore applies a group approach – ie applies the derived group Insurer Financial Strength (IFS) rating – to this rated entity. The ratings are based on an assessment of the consolidated Ageas group.

Notching

For notching purposes, the regulatory environment of Belgium is assessed by Fitch as being 'Effective', and classified as following a Group Solvency approach.

Notching Summary

IFS Ratings
For AG Insurance, a baseline recovery assumption of 'Good' applies to the IFS Rating, and standard notching was used from the IFS anchor Rating to the implied operating company IDR.
Operating company debt
Not applicable.
Holding company IDR
Not applicable.
Holding company debt
Not applicable.
Hybrids
For the two issues rated by Fitch (USD550 million perpetual subordinated bond issued in March 2013 and EUR400 million dated subordinated bond issued in March 2015), a baseline recovery assumption of "Below Average" is assumed, and they are deemed to have 'Moderate' risk of non-performance due to mandatory deferral triggers linked to a regulatory solvency event, meaning that the ratings are two notches lower than the IDR of the insurance company.

Source: Fitch

Hybrids – Equity/Debt Treatment

Hybrids Treatment

Hybrid	Amount (EURm)	CAR Fitch (%)	CAR reg. override (%)	FLR debt (%)
AG Insurance				
Fixed perpetual subordinated notes	500[a]	100	100	50
Fixed to floating dated subordinated notes	450	0	100	100
Fixed to reset dated subordinated notes	400	0	100	100

CAR – Capitalisation ratio: FLR – Financial leverage ratio
For CAR % includes portion of hybrid value included as available capital, both before (Fitch %) and the regulatory override
For FLR, % includes portion of hybrid value included as debt in numerator of leverage ratio
[a] USD550 million
Source: Fitch

Criteria Variations

None.

The Ratings above were solicited and assigned or maintained at the request of the rated entity/issuer or a related third party. Any exceptions follow below.